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CHINA Legal Bulletin

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Executive Summary

Summary of the Recent MOFCOM FDI Guidance

The Ministry of Commerce recently issued guidelines for attracting foreign direct investment in China, detailing what areas are to be encouraged and what the government should do to grow these areas. Most notably among the recommendations is the emphasis on environmental industries and high tech enterprises and the mention of involvement by foreign parties in the restructuring of State enterprises. However, it is also mentioned that mergers and acquisitions in China will be monitored more closely.

By Phenix Zheng and Mark Dahl

Disputes and Resolutions

Disputes in business are a way of life. In this article we take a look at some of the reasons why disputes arise, how to avoid them, and possible routes to resolution in China. In particular we discuss the role of negotiation, arbitration, and litigation as a means to reaching a successful outcome.

By Pavendeep Bains

Current State of Affairs in the PRC Business Scene

Mr. Shiv Morjaria, provides his insights on where China is currently and where it is going in the near future. Mr. Roos talks about the effects of the recent changes in the Labor Law and other challenges businesses face in 2008, while also addressing China's unfazed growth rate and the questions surrounding the migration of some manufacturing industries to other nations.

By Shiv Morjaria

NEWS FLASH

Next China Legal Bulletin to Focus on the PRC Labor Law and Interpretations

Shortly before the break for holidays in August, Wang Jing & Co. will publish a special edition of the China Legal Bulletin, focusing entirely on PRC Labor Law. The Bulletin will be our 4th this year and will have articles on such hot topics as overtime pay, social insurance, and severance pay. We will also include introductions of recent implementing rules given by both the State Council and the Higher Peoples Court of Guandong Province. This issue will be a must read for any manager or business owner with staff in China.

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Summary of the Recent MOFCOM FDI Guidance



Summary of the Recent MOFCOM FDI Guidance

On March 6, 2008 the Ministry of Commerce (MOFCOM) issued The Instructive Guidance on the Nationwide Work for Attraction of Foreign Investment (the **FDI Guidance**). The FDI Guidance says that analysis of trends in economic development indicate that attracting foreign investment has improved, but is still a challenge. It also mentions that the Chinese government will continue to improve the environment for foreign investment and enhance international competitiveness to keep the steady growth of foreign investment.

The FDI Guidance emphasizes that the following points are key to attracting foreign investment in 2008:

1. Governments should encourage the change in foreign investment from inviting and attracting investment to inviting and selecting investment. Therefore, local governments should set new goals and requirements for foreign investment that emphasize energy conservation, reduction of emissions, economical/efficient use of land, and a commitment to social responsibility. This will increase the quality of foreign investment and cause it to yield greater returns.
2. In order to take full advantage of any improvements to industry, local governments should implement the Catalogue for Guidance of Foreign Investment Industries (Revised 2007) formulated by MOFCOM. Including:
 - Helping foreign investors with access to new technology industries, as well as modern services, modern agriculture, and the construction of infrastructure.
 - Encouraging foreign-invested enterprises (FIE) and multinational corporations to cooperate with Chinese enterprises and science institutes to develop original innovations and local intellectual property. Investments in research and development will receive tax benefits and other incentives in order to promote upgrading the Chinese industrial landscape.
 - Encouraging enterprises with the potential to reduce emissions to cooperate with international investors to

facilitate funding and advance any technology used for energy conservation and emissions reductions.

- Traditional industries involving the making of steel, cement, electrolytic aluminum and real estate, are no longer encouraged but rather are now restricted. Furthermore, foreigners may not invest in the mining and quarrying industry. They may not explore for, or mine for important or rare resources. Lastly, industries with high energy consumption and high emissions output can not be transferred into China.

3. In order to improve the modern service industry in China, multinational corporations are encouraged to transfer their international services into China. In addition the Chinese government will continue to carry out the Thousand Hundred Ten Project, which includes four key aspects of international service outsourcing; formulating specific policies, supplying public services and strengthening human resources to relieve the conflict between supply and demand, encouraging enterprises to reach the international qualification standards issued by the State Development Bank, and strengthening the protection of intellectual property. Moreover, the Chinese government will continue to direct foreign enterprises to invest in the service industry, as well as social services that focus on improving the Chinese citizens livelihood.
4. In order to encourage foreign investment in venture capital, the government should improve the Exit Route Mechanism for Venture Capital. In addition, FIEs are encouraged to have their companies listed in China if they satisfy the listing requirements. Foreign investors are encouraged to participate in the reorganization of state-owned enterprises by means of mergers and acquisitions (M&A); however, the government will increase its supervision of M&As to safeguard the security of the national economy.

These changes to Chinese policy will open the Chinese market to foreign industries that will improve the economic and industrial growth of China. The regulations placed on investment will continue to safeguard the national economy and assuming the regulations function as intended, we can all look forward to more prosperous days for China.

By Phenix Zheng and Mark Dahl

PRC LEGISLATIVE UPDATE:

Anti-Monopoly Law to Take Effect on August 1

China's Anti-Monopoly Law will officially take effect on August 1, 2008. This move towards a more level playing field between all investors in the Chinese market, both foreign and domestic, is a welcome addition to the law of China. Some have criticized the law however, saying it is not clear enough, making it difficult to interpret and understand what the law requires. In a gesture towards transparency and a more open approach to vetting laws, the government has made drafts of the law available to the public and encouraged opinions and suggestions.

Interpretation of the Company Law Issued by Supreme Court

On May 12, 2008 the Supreme Peoples Court promulgated the *Judicial Interpretation of Some Issues Regarding the Application of the PRC Company Law*, and it became effective on May 19, 2008. This information helps to clarify issues relating to Chapter 10 on dissolution of liquidation of companies incorporated in China. The process of dissolution and liquidation for foreign-invested enterprises and domestically-owned companies, both limited liability companies and joint stock companies is described in a more structured process.

Judicial Interpretation specifically undertakes to provide enhanced rights/protection for minority shareholders and creditors in the dissolution and liquidation process of a company by allowing minority shareholder to apply for dissolution of a company if certain conditions are met and the majority has not undertaken to fix the conditions. This step towards a more regulated method for liquidation will greatly benefit companies that undertake this process in the future.



Disputes and Resolutions

When considering the legal issues that arise from the recent developments within China, one of the issues at the forefront is dispute resolution, where a foreign company is entangled in a dispute with a Chinese company. Past experience shows that disputes are not simple matters to resolve in China. When the parties concerned are from different countries, different systems of law and differences in culture must be taken into account.

In China the first step to consider when resolving a dispute is negotiation. This avoids the need to formalize the dispute and hopefully results in a settlement. It can also be less costly and time consuming than more formal methods. However, the effectiveness of this approach is very much dependant on whether the parties are willing to communicate; if there is a breakdown in communication then negotiating a settlement will likely be unsuccessful.

In the event that negotiations do not lead to a settlement or are no longer a viable option, then arbitration is another option. In order to bring a case to arbitration there should be a clause included in the contract stipulating if a dispute arises then the dispute must be brought to arbitration. If the parties do not have an arbitration clause in their contract and one of the parties does not agree to use this approach to settle the dispute then litigation is the only resort.

The main Chinese government-sponsored arbitration bodies for handling cases involving at least one foreign party are the China International Economic and Trade Arbitration Commission (CIETAC), and for maritime disputes the China Maritime Arbitration Commission (CMAC). One clear benefit of arbitration is that if the dispute is one of a highly technical nature then the arbitrators with the appropriate level of expertise can be appointed.

The last way to settle a dispute is through litigation in a Chinese court. Under Chinese law, foreign individuals and companies have the same rights to bring action in court as Chinese citizens and companies. Nonetheless, many complications can arise when taking a case to court. By looking at a recent case involving a client of Wang Jing & Co., we can see many of the difficulties in resolving a problem that a foreign company could face when he tries to resolve his dispute in China. The case involved a European client exporting goods from China to Germany. the problem arose because the client did not have a formal contract with the Chinese company supplying the goods, and there was no contract with the companys Chinese agent who dealt with all affairs concerning the shipment

of the goods. The result of this was that when our client received faulty goods, there was little evidence to support his claim. Furthermore there was not only a communication breakdown due to the language barrier, but also a lack of understanding as to what action could be taken in China against the clients supplier. The client sought to recover the cost of the faulty goods and shipping costs.

In this case the amount that the client wished to claim in damages for the faulty goods was nominal in comparison to the possible cost and time of taking the case to court. We discuss below some factors businesses should take into consideration, and could be applied as general rules to any dispute:

1. Be sure that contract terms are clear and precise. The exact terms of payment and performance standards with set time limits should be precisely stipulated, with the inclusion of a clause for dispute resolution (e.g. incorporating arbitration, or maintaining operations during a dispute). It is also important to pay careful attention to detail, for example ensuring the contracts are properly signed and stamped, and that the Chinese version of the contract has the same meaning and understanding as the English version.
2. Know exactly who your partner is and understand their past history, as this will allow you to gain a better idea of what they are like when dealing with them in business.
3. Ensure that the project is economically viable, and that the profitability of the project is based on good economic considerations.
4. Conduct a thorough risk assessment and what measures can be put into place to prevent these possible risks from occurring.

In conclusion a basic knowledge and understanding of the above can provide companies and individuals with a general understanding of how to avoid disputes from occurring in relation to business in the first place, and more importantly, to know what to do in the event there is a dispute.

By Pavendeep Bains

WANG JING & Co. UPDATE

Shipping Law Firm of the Year

At the annual ALB China Law Awards held on 25th April 2008, Wang Jing & Co. took home the award for Shipping Law Firm of the Year. The firm was also nominated for the Guangzhou Law Firm of the Year and Insurance Law Firm of the Year categories, and has been a previous winner in both, but this is the first time that it takes home the award for its traditional core area, its shipping practice.

The ALB China Law Awards is organized annually by Asian Legal Business (ALB), Asia's leading magazine for legal professionals.

Contributions on Insurance and Reinsurance Law

In recognition of it's experience and expertise in dealing with contentious and non-continuous issues relating to a broad range of insurance issues, Wang Jing & Co. was recently asked to contribute to Getting the Deal Through: Insurance and Reinsurance. The publication, which began distribution in May 2008, took contributions from law firms from all over the world with dedicated insurance practices, and collected these to form a comparative bundle on the law of insurance and reinsurance, and regulations of the industry. The article for China was written by Shanghai managing partner Mr. Zhong Cheng and Shenzhen partner Mr. Sun Jingliang.

Wang Jing & Co. is proud to be associated with this publication, and encourages companies interested in insurance law to visit www.gettingthedealthrough.com for more information.

Current State of Affairs in the PRC Business Scene



Current State of Affairs in the PRC Business Scene

The Challenges

Doing business in China is not as simple as finding a nice office in Guangzhou and a nearby manufacturing facility. Foreign firms in China face a number of obstacles, including an opaque bureaucracy, competition from state-supported enterprises, the shortage and cost of highly skilled labor, piracy of intellectual property, and a developing legal system.

In addition, with the introduction of strict labor laws, efficiency may decline and foreign companies will no longer benefit from the current market flexibility. It is clear is that the new legislation would cause companies to incur increased costs if followed by the letter.

Furthermore, China is not immune from the slowdown in the global economy. It is already experiencing lower demand from its major trading partners such as the United States and feeling the inflationary pressures of soaring commodities such as oil and food. In addition the effects of the falling US dollar and growing competition from other emerging economies such as Vietnam are further factors that will affect Chinese competitiveness in the short and medium term.

More growth in China

However, despite these commercial and legal uncertainties of doing business in China, China undoubtedly remains a force to be reckoned with. It is not surprising that international law firms are competing rigorously to service the needs of multinational and Chinese clients.

While many developed nations are currently nursing trade deficits and in the mist of an unprecedented credit crunch, China is awash with liquidity. Chinas foreign currency reserves are now more than \$1.6 trillion. This is feeding domestic development and driving outbound

foreign investment. In 2006 approximately 5,000 Chinese entities established almost 10,000 companies in 172 countries. Chinese private and state enterprises have been propelled onto the world stage by the audacious acquisitions of well-known international brands such as IBM and MG Rover. Chinas stock markets saw 160 company launch IPOs in 2007 (roughly the same as the United States), with a cumulative value of more than \$50 billion.

Moreover, the 2008 guidance on FDI issued by the Ministry of Commerce outlines numerous initiatives further attracting foreign investment. Examples of this include improving exit route mechanisms for venture capitalist as well as tax benefits for investments in research and development. Yet, similar initiatives from neighboring counties must also be noted as the threat of investors switching production to Vietnam for example cannot be underestimated. For instance foreign investment soared 47% to nearly \$10.2 billion last year. This is further forecasted to double to \$20bn this year with firms such as Intel (the worlds largest semiconductor maker) starting construction on a \$1 billion chip assembly plant in the countrys southern business hub.

Nonetheless, the reality remains that China is the second largest economy in the world. It is predicted that if Chinas GDP grows by 8% per annum (averaged 10% since reforms) it will be three times larger than the United States by 2030 and five times larger by 2050. While the strengthening of its employment laws may have a detrimental impact on China's popularity among foreign investors, it is hard to imagine a situation where those manufacturing jobs already well rooted in China could return to the United States or Europe. Ultimately, the region and specifically China is likely to remain profitable.

By Shiv Morjaria

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This newsletter is published by the Corporate & Commercial Group of Wang Jing & Co, a PRC law firm assisting Chinese and multinational clients in business operations in China and abroad.

WANG JING & Co. UPDATE:

Senior Consultant Maarten Roos Moves to Shanghai

To further develop Wang Jing & Co's general corporate practice in Shanghai, Senior Consultant Maarten Roos has joined the firms Shanghai Office as of 1 July 2008. While Mr. Roos will continue to visit the Guangzhou headquarters every month to supervise the FDI and IP teams and advise his Clients in southern China, his presence in Shanghai will enable the Firm to further develop in-depth relationships with clients and referral partners based in the Yangzhou River Delta.



Mr. Roos advises foreign clients on a wide range of legal and commercial issues, and focuses on foreign direct investment projects, intellectual property protection and general dispute resolution. In the latest Asia Leading Lawyers survey, he was nominated for the General Corporate Practice and Dispute Resolution categories.

Asia Leading Lawyers Survey

Wang Jing & Co. is proud to announce that several of its legal professionals were among those nominated in Asialaw annual survey of Asia Leading Lawyers 2008. Professionals from our Guangzhou, Shanghai and Tianjin offices were chosen for their expertise in Shipping, General Corporate Practice, Dispute Resolution and Intellectual Property, signifying the firms growing depth and geographical spread, as well as the high level of client satisfaction.

Nominated professionals: Wang Jing, Chen Xiangyong, Zhao Shuzhou, Shen Xiangman, Zou Zongcui, Liu Chunhua, Maarten Roos